WORK AND RETIREMENT: OPTIONS FOR CONTINUED EMPLOYMENT OF OLDER WORKERS

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PREFACE

Several issues now before the Congress deal with the causes or consequences of the growing number of older persons who are not employed. This paper, requested by the Senate Budget Committee, describes the present and future elderly populations and how demographic changes will affect the labor market, the economy, and the federal budget. It examines the determinants of retirement decisions, how those choices are affected by federal programs and policies, and options to facilitate continued employment by older persons.

This study was prepared by Bruce Vavrichek of the Congressional Budget Office's (CBO) Human Resources and Community Development Division, under the supervision of Nancy M. Gordon and Martin D. Levine. Many individuals provided valuable technical and critical contributions, including Stephen R. McConnell, Paul Cullinan, Jan Lilja, Marilyn Moon, Malcolm Morrison, Lawrence Olson, and Carl Schmertmann. Patricia H. Johnston edited the manuscript. Mary V. Braxton typed the several drafts and prepared the paper for publication.

In accordance with CBO's mandate to provide objective and impartial analysis, this paper contains no recommendations.

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Director

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CONTENTS

CONTENTS (Continued)

PAGE

TABLES

FIGURES

96-296 O - 82 - 2

SUMMARY

The aging of the population in the years ahead--and especially the increase in the number of older persons who are not employed--has significant implications for those persons, for the economy as a whole, and for the federal government as a provider of retirement income. Persons retiring from the work force not only experience potentially large reductions in income but also may contribute to other sources of declining labor force growth in the future--a trend that could result in lower national output. Budgetary concerns arise both because of increased outlays for income support and because a smaller work force means fewer people to pay for these and other services.

In light of these concerns, the Congress may wish to review those federal policies that are partly responsible for reduced employment by many older persons. Further, it may want to consider options to enhance the employment opportunities of those older Americans who can and choose to continue to work.

THE GROWING NUMBER OF NONEMPLOYED OLDER PERSONS

The number of people 65 and older is continuing to increase as a share of the total population. In 1980, one in nine--or 24 million--Americans were 65 or older, compared to one in twelve in 1950 (see Summary Table 1). The elderly population will increase only moderately over the next few decades, but soon after 2010 its size will grow dramatically. By 2030, nearly one in five--or almost 56 million--Americans will be 65 or older.

At the same time, the fraction of older persons in the labor force is declining. Between 1950 and 1980, the portion of those 65 and older in the labor force fell from 24 percent to 13 percent, primarily as a result of increased retirement by elderly men. Since 1970, the labor force participation rate of persons 55 to 64 has also fallen slightly--from 62 percent to 56 percent.

These declines in labor force participation may not continue, however, because more older persons may need to work to compensate

SUMMARY TABLE 1. THE NONEMPLOYED POPULATION 65 AND OLDER, SELECTED CALENDAR YEARS 1950 TO 2030

	1950	1980	2005	2030
Number of Persons 65 and Older (In millions)	12.4	23.7	33.1	55.9
Percent of Persons 65 and Older Employed	23.4	12.3	12.3[a]	12.3[a]
Nonworking Persons 65 and Older as a Percent of Total Population	6.2	9.5	10.6[a]	15.9[a]

SOURCES: Bureau of the Census, "True Level Population Projections" (1977); Employment and Training Report of the President, 1980; Bureau of Labor Statistics, Employment and Unemployment: A Report on 1980, Special Labor Force Report 244 (April 1981); and CBO tabulations based on the Bureau of the Census, Current Population Survey (March 1980).

a. Assumes the same labor force participation rate as in 1980.

for the effects of inflation on their incomes, and because an expected reduction in the growth of the overall labor force may increase the demand for older workers. Nonetheless, even if the portion of elderly persons in the work force does not change from its 1980 level, by 2030 almost 16 percent of the population--or 49 million persons--will be over 64 and not employed.

ECONOMIC AND BUDGETARY IMPLICATIONS

Increasing numbers of nonworking older persons could reduce the amount of goods and services produced in the economy as well as personal incomes. This decreased production could also put upward pressure on prices and increase inflation. The smaller labor force of older workers probably would reduce overall unemployment, however, because many jobs not taken by older persons would go to younger ones.

As the number of nonworking older persons grows, the federal budget could also be affected by increased outlays for retirement programs and decreased income and payroll tax revenues. For example, when a person stops working and begins collecting Social Security benefits, annual outlays for Social Security increase on average about $4,800 and Social Security and income tax revenues decrease by over $2,000. Federal spending on retirement income for persons 65 and older alone already represents 19 percent of the budget--or over $130 billion in fiscal year 1982--and spending for their health care amounts to over $48 billion, or 7 percent. This spending has increased in recent years not only because of the growing size of the elderly population, but also because of increased benefits, expanded coverage, and more earlier retirements.

OPTIONS FOR CONTINUED EMPLOYMENT BY OLDER WORKERS

The federal government already significantly influences the work and retirement decisions of older persons; taken together, federal programs and policies facilitate and promote retirement. Because of the implications of demographic and labor market trends for the economy and federal budget, questions arise about whether there is too great an incentive to retire early, and whether there are too few policies to facilitate continued employment. The Congress might wish to consider policy changes that would encourage older persons to continue in, or reenter, the workforce. Options could include the following:

- Modify the Social Security system;
- Revise existing regulations for employers; and
- Change other labor market programs that affect the supply of and demand for older workers.

The largest gains in employment--and the sharpest drop in federal outlays--probably would result from options that penalize retirement (see Summary Table 2). Financial incentives for continued work might or might not result in significantly greater employment by older workers, but would necessarily increase federal outlays substantially because those already working would receive increased benefits. Smaller increases in employment could also be obtained from other options involving relatively small federal outlays or changes in federal regulations. Finally, any option

SUMMARY TABLE 2. COMPARISON OF SELECTED OPTIONS TO INCREASE EMPLOYMENT BY OLDER PERSONS

Option	Estimated Increase in Labor Force	1983 Estimated Direct Federal Expenditure Increases or Revenue Losses[a]
Modify Social Security		
Increase Ages of Normal and Early Retirement in Social Security to 68 and 65, Respectively[b]	If fully implemented, eliminates benefits for over 2 million retired workers 62-64 and their dependents, thus encouraging continued employment.[c]	If fully implemented, reduces outlays by about $17 billion.
Restrict Maximum Age of Social Security Earnings Test to 64	About 150,000 workers, plus increased hours worked for over 200,000 workers.	Increases outlays by $3.5 billion, compared to test with maximum age 69.
Revise Regulations for Employers		
Require Continued Accrual of Private Pension Benefits	50,000 male workers 60-70 by year 2000.	None.
Prorate Private Pension Benefits for Post-Retirement Work	About 20,000 workers.	None.
Eliminate Mandatory Retirement at Age 70	195,000 male workers 60-70 by year 2000.	None.
Change Other Labor Market Programs		
Establish an Employment Tax Credit for Low-Income, Unemployed Older Persons	75,000 workers, assuming 5 percent of those eligible use the credit.[d]	Reduces revenues by $125 million.
Provide Work Experience for Older Persons	50,000 workers.[d]	Increases outlays by $175 million.
Provide Retraining for Skilled Older Workers	About 30,000 workers 60-64.[d]	Increases outlays by $40 million.

a. Does not include offsetting revenue increases resulting from additional payroll and income taxes.

b. It is unlikely that this change would be implemented quickly and 1983 estimates are presented only to give an idea of the impact when fully implemented.

c. The number of these persons who would enter the labor force is thought to be large, but is not known.

d. Includes some workers who would have been hired without this program.

that increases employment would also increase federal revenues from payroll and income taxes, thus offsetting part of the cost.

It is also important to note that the success of all these options in generating employment would depend in large part on the overall strength of the economy. While sustained economic growth is desirable for many reasons, increased growth could especially help the employment of older workers. Most currently employed older persons are in those industries and occupations in which greatest future growth is apt to occur, and the trend toward a service and high-technology oriented economy could generate the kinds of jobs that they could fill. It could also increase the demand for part-time workers and provide additional opportunities for those older persons who do not wish to, or cannot, work full time. Sustained economic growth could also reduce the extent to which employment of older workers would displace younger persons.

Modify the Social Security System

Features of Social Security provide both financial incentives and disincentives for continued work by older persons; however, aside from problems of poor health, this system is probably the most important factor in inducing many older persons to retire. Consequently, options for modifying Social Security--changing the age-benefit structure and the earnings test--probably would most significantly affect the number of employed older persons.

Change the Social Security Age-Benefit Structure. Changes in the relationship between the age of retirement and the level of Social Security benefits could penalize earlier retirement, promote delayed retirement, or both. Currently, full retirement benefits are available at 65; benefits are reduced for retiring between 62 and 65 and increased for delaying retirement up to 72. Most proposals to alter these provisions--including those to increase the ages of entitlement for normal and early retirement and to reduce benefits further for early retirement--have been offered as solutions to the financial problems of the Social Security trust funds. They would also be effective, however, in inducing continued employment of older persons. Although these changes probably would not be introduced for several years, an indication of their impact can be obtained by considering their effect if implemented in 1983. For example, if increases in the early and normal retirement ages to 65 and 68, respectively, were fully implemented in 1983, benefits to over 2 million retired-worker beneficiaries 62 to 64 and their dependents would be eliminated, for a savings of over $17 billion in federal outlays. Reducing benefits for retirement at 62 to 55 percent of the full amount--as was proposed by the Administration in 1981--could increase employment by as many as one million persons 62 to 64 and could also result in large federal savings. Other proposals, such as increasing the benefit for delayed retirement, would encourage later retirement, but also would raise Social Security outlays.

Change the Social Security Earnings Test. The Social Security earnings test reduces benefits to recipients 62 through 71 when their earnings exceed certain limits, thereby providing a strong disincentive for work beyond that limited amount. Options for modifying the test include restricting the ages of its application, increasing the earnings limits, or completely eliminating the test. Each of these changes would stimulate employment both by those currently receiving reduced benefits because of the test and by those who have restricted their employment to avoid losing benefits. They would worsen the financial position of the Social Security trust funds, however, by increasing benefit payments. Removing the test for those 65 and older, for example, could increase the work effort of over 350,000 elderly persons in 1983, but would increase Social Security outlays by an estimated $3.5 billion.

Revise Existing Regulations for Employers

Through existing provisions in private pension regulations and anti-age discrimination statutes, employers can effectively limit the amount of work performed by some older persons. Certain changes in these federal regulations could provide additional opportunities for older persons to continue their employment. Each of the options described below would not add to direct federal costs but could impose costs on employers. These options could generate between 20,000 and 200,000 additional jobs for older workers.

Require Continued Accrual of Private Pension Benefits. Under current law, federally regulated private pensions are allowed to cease accrual of benefits once workers become eligible for normal retirement. In one major study, nearly half of the plans had such limits. To reduce this work disincentive, the Congress could specify that plans covered under the Employee Retirement Income Security Act (ERISA) must continue pension accrual for work beyond the date of pension eligibility.

Increase Allowable Retirement Work Under Private Pensions. ERISA regulations allow private pensions to withhold all benefits from retirees who work more than 40 hours per month in so-called prohibited employment--which, depending on the plan, includes work for the same firm or in similar jobs in the same industry and area. This rule can effectively restrict employment once pension benefits are accepted. An alternative would be to allow only prorated reductions in benefits according to the amount of continued employment--for example, reducing benefits by one-half for a beneficary who works half time.

Eliminate Mandatory Retirement Because of Age. Removing the current age 70 upper limit on mandatory retirement under the Age Discrimination in Employment Act (ADEA) probably would also increase the employment of older workers. This change would require some employers to reevaluate extended work possibilities on the basis of employees' abilities, but would also ensure that employees would not have their careers terminated solely because of age. The impact of this change is uncertain, however, because it would depend in large part on future characteristics of private pension plans, since most mandatory retirement provisions apply to jobs covered by these plans.

Change Other Labor Market Programs

Providing employers with a wage subsidy for hiring certain older persons or assisting older persons to acquire skills valuable in expanding areas of the economy could increase employment prospects for these workers. Depending on the services or incentives provided, federal costs could range up to $3,500 per participant and could assist 30,000 to 75,000 older persons to obtain employment. Because participants in these programs would be given an advantage over younger nonparticipants, however, part of their increased employment probably would occur through displacement of younger workers.

Provide Employment Tax Credits for Older Workers. Offering a wage subsidy to employers of certain older persons could increase the demand for these workers. Such a subsidy could be provided either as a direct payment to the employer or as a tax reduction. It could be offered, for example, to employers of unemployed low-income older persons and could be provided through the existing Targeted Jobs Tax Credit.

96-296 O - 82 - 3

Assist Inexperienced Workers. Because of changing family situations and responsibilities, many older persons with little employment experience have the desire--or need--to enter the workforce. The federal government could assist these persons in obtaining so-called entry level jobs by providing work-experience and job-search assistance.

Assist Experienced Workers. Some older persons who have considerable employment experience but lack the opportunity or ability to continue in their former occupations could also be assisted in finding new employment. Such assistance could include job counseling to match their skills with employer demands and--when few opportunities could be found--help in obtaining vocational-technical training and limited educational enhancement to meet the skill requirements of available jobs.

CHAPTER I. INTRODUCTION

Existing federal policies both facilitate and encourage retirement through the provision of retirement income and other policies that reduce the rewards for working. As the number of older persons and their share of the population increase in the years ahead, current retirement patterns could have substantial effects not only on those persons but also on the economy and federal budget as well. For these reasons, the Congress might wish to review how federal policies affect retirement decisions and how they might be changed to enhance employment opportunities for those older persons who both were able and chose to continue working.

The Congress is now considering several issues that involve the causes or consequences of the growing number of nonemployed older persons. The benefit and financing provisions of the Social Security system continue to be of major concern. Several bills currently pending in the Congress highlight the ongoing review of federal regulation of private pensions under the Employee Retirement Income Security Act (ERISA). This year's reauthorization of employment and training legislation raises questions about the continuation of programs targeted on older workers. Finally, the Administration and several members of Congress have proposed amending the Age Discrimination in Employment Act to abolish the current allowable mandatory retirement age of 70.

THE AGING OF THE POPULATION

The importance of issues relating to work and retirement policies is based on the large and growing size of the older population. Today, more than one in five Americans are above 54 and one in nine--or nearly 25 million--are 65 or older (see Table 1). Over 9 million persons are 75 or older. In this paper, the term "older persons" generally is used to refer to those 55 and above, while "elderly" is reserved for those 65 and older.[1]

1. An appropriate definition of the age group that constitutes the "elderly" population depends on the aspect of behavior of (Continued)

TABLE 1. DEMOGRAPHIC CHARACTERISTICS OF THE POPULATION, BY AGE GROUP, MARCH 1981

Demographic Characteristics	All Ages	Age Group 0-54	55-64	65-74	75+
Number of Persons (In thousands)	225,242	178,851	21,705	15,523	9,163
Distribution (In percents)					
Sex					
Male	48.4	49.7	46.7	43.4	36.8
Female	51.6	50.3	53.3	56.6	63.2
Marital status					
Married	45.0	40.0	74.8	63.1	40.6
Widowed	5.7	0.8	11.7	26.3	51.2
Other	49.4	59.2	13.5	10.7	8.2
Geographical region					
Northeast	21.6	21.0	23.9	23.4	23.1
North Central	25.8	25.9	25.0	25.0	27.0
South	33.3	33.4	32.6	34.2	32.7
West	19.3	19.7	18.5	17.3	17.2

SOURCE: CBO tabulations based on the Bureau of the Census, Current Population Survey (March 1981).

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1. (Continued) interest. Age of retirement and the age at which significant declines in health occur are the usual criteria that define old age. The typical use of the term elderly for those 65 and older is without strong factual support but has become ingrained in society. Adoption of 65 as the retirement age for Social Security helped to make that the standard age of retirement. With the increased incidence of early retirement in recent years, however, the term elderly is sometimes extended to include the 55 to 64 age group. Eligibility for private pension benefits at ages after 55 and the consequent changes in life style after acceptance of these benefits have popularized 55 as the beginning of old age. Conversely, with increases in life expectancy and improvement in the health of many older citizens, some maintain that the term elderly should apply only to those 68 or 70 and older.

Women constitute almost 60 percent of the 65-and-older population and one in three persons over 64 is widowed. Geographically, compared to persons of all ages, there are proportionately more elderly persons in the Northeast and fewer in the West.

Over the next 30 years, the size of the elderly population is expected to grow at about the same rate as the entire population, but after about 2010, both the number of elderly persons and their share of the total population are projected to increase dramatically. (This report uses the intermediate assumptions in population projection reports by the Census Bureau and Social Security Administration.)[2] Approximately 20 million persons will reach 65 during each of the three decades from 1980 to 2010 (see Figure 1); however, that number will rise to over 30 million persons in the decades after 2010. The share of elderly in the population will remain at about 12 percent until 2010 and then probably will increase to over 18 percent by 2030 (see Figure 2). These trends reflect the aging of the large post-World War II baby boom and increases in life expectancy (see Table 2).

The sharp increase in the elderly population will result in a decline in the ratio of the working- to nonworking-age population --and, therefore, in a decline in the number of persons contributing to the Social Security system compared to the number of beneficiaries. Between 1980 and 2030, the ratio of the number of persons 20 to 64 to those over 64 is projected to decline from over 5-to-1 to 3-to-1. Similarly, the average number of workers per Social Security beneficiary is projected to decline from 3.7 in 1981 to 2.2 in 2030. The ratio of persons aged 20 to 64 to those who are either elderly or under age 20 will change by a lesser amount, in part because of a decrease in the size of the under-20 population.

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2. See Bureau of the Census, "True Level Population Projections" (1977); and Social Security Administration, Social Security Area Population Projections, 1981, Actuarial Study Number 85 (July 1981). These projections are based on several assumptions that, together, determine their accuracy. The intermediate assumptions in both sets of forecasts--the ones used in this analysis--include an average fertility rate of 2.1 children per woman, projected life expectancies increasing somewhat in future years, and annual net immigration of 400,000 persons.